

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

NORTH SHORE GAS COMPANY)	
)	
Proposed General Increase)	No. 07-0241
In Rates for Natural Gas Service)	
)	
)	
THE PEOPLES GAS LIGHT AND)	
COKE COMPANY)	
)	
Proposed General Increase)	No. 07-0242
In Rates for Natural Gas Service)	

**CUB REPLY BRIEF ON THE ISSUE OF
PEOPLES GAS LIGHT AND COKE COMPANY'S
PROPOSED RIDER ICR**

CITIZENS UTILITY BOARD

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Pursuant to Section 200.800 of the Rules of Practice of the Illinois Commerce Commission (“Commission” or “ICC”), 83 Ill. Admin. Code 200.800, and the briefing schedule set by the Administrative Law Judges (“ALJs”), the CITIZENS UTILITY BOARD (“CUB”), by its attorney, submits its Reply Brief on the issue of Peoples Gas Light & Coke Company’s (“Peoples,” “PGL” or the “Company”) proposed Rider ICR in this proceeding. For the reasons described in detail below, CUB opposes adoption of Rider ICR, as well as each of its alternatives.

ARGUMENT

CUB, Staff and the Attorney General (“AG”) are all in agreement that Rider ICR should be rejected by the Commission as illegal and an impermissible violation of established legal and regulatory criteria. Specifically, CUB, Staff and the AG all argue that Rider ICR violates the prohibition against single issue ratemaking, as well as generally-accepted regulatory and legal

criteria required to warrant extraordinary rate treatment of ordinary rate base additions. *See* CUB Initial Br.; Staff Initial Br. at 190; AG Initial Br. at 89. Furthermore, CUB, the AG, and Staff all concluded that Rider ICR represents a dramatic, unacceptable and illegal departure from traditional test year ratemaking policy. CUB Initial Br. at 4, Staff Initial Br. at 190, AG Initial Br. at 73.

All parties agree that, in order to warrant the exceptional rate treatment Rider ICR represents, costs must be unexpected, volatile or fluctuating and significant in nature. CUB Initial Br. at 6; Staff Initial Br. at 190; AG Initial Br. at 88. Rider ICR does not, however, address or respond to issues of volatility or uncertainty or costs beyond the control of management. In fact, as CUB argued in its Initial Brief, costs are well within the control of management, as evidenced by the fact that the Company has been able to successfully manage the costs of its existing main replacement program, while simultaneously making numerous improvements in its operations to create efficiencies and consequently avoid a rate case for 12 years. CUB Initial Br. at 6.

Staff, the AG and CUB further all agree that Rider ICR is impermissible under Illinois law. First, Rider ICR violates the PUA's requirements that all utility rates and charges are determined to be just and reasonable before being included in rates. 220 ILCS 5/9-101. Second, Rider ICR violates the PUA's requirement that any additions to existing facilities or plant be prudent and used and useful in providing utility service to the utilities' customers. 220 ILCS 5/9-212. Third, Rider ICR violates the PUA's requirement to provide least cost service. *See* CUB Initial Br. at 9-14. Finally, it violates the prohibition against single-issue ratemaking under Illinois law. While potential changes in one or more items of expense or revenue may be offset by increases or decreases in other such items, single-issue ratemaking considers those changes in

isolation, ignoring the totality of circumstances. *A. Finkl & Sons Co. v. Illinois Commerce Comm’n*, 250 Ill. App.3d 317 at 325(1st Dist. 1993). Rider ICR considers changes to components of the revenue requirement in isolation by allowing infrastructure to be added to rate base without consideration of the impact of those additions on operation and maintenance savings and the Company’s rate of return. *See* CUB Initial Br. at 13. Rider ICR thus violates Illinois law’s test-year principles by increasing monthly rates without considering other offsetting rate components and without Commission review or approval.

Furthermore, as CUB argued in its Initial Brief, the Company has not substantiated a need for its proposed accelerated program to replace its cast iron and ductile iron mains (“CI/DI”) that would impose costs on consumers above the costs of other plant additions to rate base. The Company’s justification for its proposed Rider ICR is a desire to avail itself of unknown future opportunities to coordinate with the City of Chicago on large projects where it could replace CI/DI mains. NS/PGL Initial Br. at 122. However, as pointed out by Staff, “since 1981 Peoples Gas has been able to conduct a main replacement program without the need of a rider, demonstrating that it is possible to plan and budget for a main replacement program despite the existence of special projects and events.” ICC Staff Exhibit 8.0 at 37-38, L. 775-785. Further, the benefits do not appear to be enough for the Company to commit to less frequent rate cases if its proposal is adopted. Staff Initial Br. at 192.

Moreover, the current main replacement program has been demonstrated to allow the Company to maintain a safe and reliable distribution main system. *See* CUB Initial Br. at 10-11. Additionally, the Company’s ongoing CI/DI replacement program has successfully allowed it to upgrade its distribution mains system at a reasonable pace while allowing the Company to experience healthy returns. If it chose to pursue an accelerated program, Peoples Gas could do

so without the use of extraordinary rate treatment while maintaining the balanced test year review process. If these additional infrastructure costs were approved in a rate case, rates would be symmetrical, where rate base, operating revenues, expenses and the cost of capital are properly matched, and the Commission has ample time to review and consider the prudence of the investments, and associated O&M savings, so that customers are not unduly harmed. GCI Ex. 4.0 at 50, L. 17-23.

In its Initial Brief, Staff made clear that it remains opposed to any rider recovery of basic infrastructure costs. Staff Initial Br. at 190. Staff's position is that Peoples Gas' proposal for rider recovery of plant costs should not be approved, but Part 656 ("Qualifying Infrastructure Plant" Rider or "Rider QIP") provides a reasonable starting point should the Commission decide that rider recovery of plant costs is appropriate. Staff Initial Br. at 197. However, the AG correctly pointed out that the 5% cap on the surcharge proposed by Staff under its Rider QIP and agreed to by the Company is essentially meaningless. AG Initial Br. at 86-87. The cap amounts to a license to spend \$123 million when its spending on distribution main, services, meter purchases and meter installations during the test year amounted to only \$32.5 million. Therefore, not only is it unlikely the Company will reach the 5% cap, but in the unusual circumstances that it would make such extraordinary investments, it could simply file a new rate case to include any additional expenditures above the cap in base rates. The cap will not operate to restrict Peoples' capital spending in any meaningful way. In addition, the fact remains that even with a cap in place, the opportunity to recover incremental investments between rate cases gives the Company an incentive to spend more. Staff Initial Br. at 195.

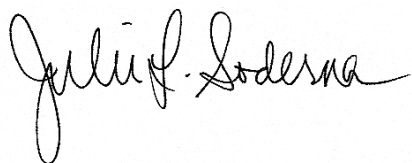
While Staff's proposed Rider QIP improves upon certain aspects of the Company's Rider ICR, no rider could cure the inherent legal and policy infirmities associated with rider recovery of basic infrastructure costs. Thus, the Commission must reject Rider ICR, the Company's Alternative Rider ICR and Staff's Rider QIP as violating the PUA's requirements that all rates are just and reasonable and all new plant prudent, used and useful, as well as the prohibition under Illinois law against single-issue ratemaking, absent a showing that the costs are large, volatile and unexpected. Peoples failed to make the requisite showing and therefore failed its burden to demonstrate that its Rider ICR is legally permissible.

WHEREFORE, for the reasons stated herein, CUB respectfully requests that the Commission reject the Company's proposed Rider ICR, its Alternative Rider ICR and Staff's proposed Rider QIP for the reasons stated in CUB's Initial and Reply Briefs on the issue of Peoples' Proposed Rider ICR.

Dated: October 23, 2007

Respectfully Submitted,

THE CITIZENS UTILITY BOARD

By: 
One of its Attorneys

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